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No. 85-555

In The
Supreme Court of the United States
October Term, 1985

BANKERS TRUST COMPANY,

Petitioner,

vs.

THELMA T. METGE, Executrix of the Estate of August Metge, and ELIZABETH G. SHEPARD, on behalf of themselves and on behalf of all others similarly situated,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals For the Eighth Circuit

BRIEF IN OPPOSITION

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QUESTION PRESENTED

SHOULD THIS COURT GRANT CERTIORARI WHEN THE DECISION OF THE COURT OF APPEALS IS NOT IN CONFLICT WITH DECISIONS OF OTHER COURTS OF APPEALS OR WITH PRIOR DECISIONS OF THIS COURT, IS INTERLOCUTORY AND AFFECTS ONLY THE PARTIES TO THIS ACTION, AND IS BASED UPON A FACT QUESTION IN THE CONTEXT OF APPROPRIATE SUMMARY JUDGMENT STANDARDS CORRECTLY APPLIED.

PARTIES TO THE PROCEEDINGS

Plaintiffs named in the caption in this case are representing themselves and a class of approximately 635 individuals similarly situated which has been certified by the District Court. The Appendix to Plaintiffs' Cross-Petition For Writ of Certiorari filed contemporaneously herewith contains a list of members of the Plaintiff class.

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BRIEF IN OPPOSITION

Respondents Thelma T. Metge, Executrix of the Estate of August Metge, and Elizabeth G. Shepard, on behalf of themselves and all others similarly situated ("Plaintiffs"), respectfully oppose the Petition for Writ of Certiorari to review the opinion and judgment of the United States Court of Appeals for the Eighth Circuit entered in the above-captioned case on May 15, 1985.

OPINIONS BELOW

The opinion of the Court of Appeals is reported at 762 F.2d 621 (8th Cir. 1985). The opinion of the District Court is reported at 577 F.Supp. 810 (S.D. Iowa 1984). Both opinions are reproduced in the Appendix to the Petition for Writ of Certiorari.

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JURISDICTION

See Petition for Writ of Certiorari, at page 2.

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PROVISIONS OF STATUTES AND RULES INVOLVED

See Petition for Writ of Certiorari, at pages 2-3.

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STATEMENT OF THE CASE

Pursuant to Sup. Ct. R. 34.2, Respondents adopt the two paragraphs of the Petition entitled "Statement of the Case." The sole correction to be noted is that while Bankers Trust Company ("BTC") is a named defendant in this action, its officers and directors are not.

Statement of Facts

It is important to understand that this action involves complicated and voluminous facts. BTC's conduct can only be understood against the backdrop of its long-standing relationships with IEI, the primary violator, and predecessor borrowers. Because of the complexity of this case, as well as the necessity of proof by circumstantial

evidence and inference, it is essential to provide a more complete, detailed and accurate picture of the facts than is contained in BTC's petition. A concise summary of the voluminous record evidence is therefore provided.

A. IEI and IMF—Background and Primary Violation

Investors Equity, Inc. ("IEI") was an Iowa corporation formed in the early 1960's to buy and service real estate contracts on low-cost homes. In 1969, because of dwindling profits and a desire to move IEI to more "high-risk, high-return" ventures, IEI formed Investors Mortgage & Finance Co. ("IMF"), a thinly-capitalized subsidiary corporation, to raise venture capital for IEI by the public sale of unregistered, unsecured, one-year renewable, promissory note-type securities called "Thrift Certificates". Beginning in 1970 IEI also issued its "Thrift Certificate Guarantee Bonds" which "unconditionally guaranteed" the Thrift Certificates. Initially IEI traded real estate contracts to IMF in return for Thrift Certificate proceeds, but by 1970 IMF merely loaned the Thrift Certificate proceeds to IEI in return for IEI's unsecured promissory notes. (By its bankruptcy in 1974 IMF's assets were mostly worthless IEI notes.) During the next several years IEI had no problem selling Thrift Certificates or finding "high-risk" investments. By 1971 IEI owned two unsuccessful lake development projects and a "disaster" of a commercial office project, and by 1974, the year of IEI's bankruptcy, the outstanding balance of Thrift Certificates was $1,500,000. IEI's violations of the anti-fraud provisions of the Federal securities laws were conceded by BTC in this summary judgment proceeding. They include fraudulent misrepresentations (non-existent collateral and fictitious use of Thrift Certificate proceeds)

and numerous non-disclosures of material facts, *e.g.*, financial condition of IEI/IMF, the need for and use of Thrift Certificate proceeds and BTC's unusual "loan" activities.

B. Plaintiffs

Plaintiffs are 635 holders of worthless Thrift Certificates and Thrift Certificate Guarantee Bonds. Their aggregate investment is $1,500,000, and their average individual investment is under $3,000. They have received none of their principal and only a few dollars of their interest. They are primarily retired persons, farmers, teachers, artisans and trades people.

C. History of MIL

Mid-Iowa Lakes Corporation ("MIL") was an Iowa corporation formed in the mid-1960's to develop Lake Panorama, a recreational lake development project near Des Moines. BTC was its stock transfer agent and the escrow agent for an early stock offering. Times were always bad for MIL. Its lake project was ill-conceived; its management was poor; its losses were large and constant; its lawsuits were many; and it never had enough money to pay its bills or complete its amenities.

D. Woodland Debt—Origin of BTC's Losses

Woodland Corporation ("Woodland") was an Iowa corporation operating in Des Moines in the 1960's. BTC was its depository bank, primary lender and stock transfer agent. In 1967 BTC was in trouble on some large loans to several Des Moines drug companies. With encouragement and acquisition financing from BTC, Woodland purchased the drug companies and restructured and assumed their

BTC debt ("Woodland Operations Loans"). The drug companies did even worse under Woodland, and by 1968 Woodland was in trouble and the Woodland Operations Loans were in substantial default. In late 1968, despite its financial woes, Woodland decided to purchase a controlling block of stock in MIL ("MIL Stock") and to raise money therefor by the public sale of Woodland debentures and warrants. BTC, who was aware of MIL's many problems, refused to consent to the transaction until Woodland agreed that a large part of the debenture proceeds would be used to reduce the Woodland Operations Loans. BTC then advanced $180,000 of the purchase price of the MIL Stock, loaned acquisition money to several debenture purchasers and disseminated the warrants. In late 1969, with the drug companies folding and Woodland hopelessly insolvent, BTC demanded and received from Woodland the MIL Stock as additional collateral for the Woodland Operations Loans. In February of 1970, as BTC was repossessing the drug companies' inventories, BTC demanded and received from Woodland an irrevocable and unlimited proxy to vote the MIL Stock. A few days later Woodland dumped the drug companies in bankruptcy, but, on BTC's "advice", Woodland stayed out of bankruptcy itself to help BTC find a buyer for the MIL Stock. (Some Woodland directors were beholden to BTC on other loans.) BTC knew it was in a "bad situation" on the Woodland Operations Loans and that its "only chance" to avoid a huge loss was to sell the control block of MIL Stock for a large sum of money. BTC also knew that selling the MIL Stock would not be easy—very few companies were interested in lake projects, especially ones with MIL's problems.

E. Sale of MIL Stock and Transfer of Woodland Debt

During the next twelve months BTC did what it could to stabilize MIL while it searched for a buyer for the MIL Stock. MIL was in dire need of $1,500,000 to pay large debts and immediate operating expenses, but all it could find was a $950,000 mortgage loan from an Omaha bank. "Purely to keep everything afloat" and "to bail out" MIL, BTC approached the Omaha bank and got it to increase the loan to $1,450,000 in return for a $500,000 BTC participation. BTC also reshaped MIL's management. BTC's president wanted MIL to add some directors and create an executive committee and when MIL balked he appeared at its January 1971 board meeting, armed with the irrevocable proxy taken in 1970 "to assure good management" (*supra* at 5), and the changes were made.

By February of 1971 BTC had interested only two potential purchasers in the MIL Stock. One was MIL itself (actually, dissident directors), and the other was IEI. Both were willing to pay approximately $950,000 (the balance of the Woodland Operations Loans), and both needed BTC to finance most of the purchase price. Although IEI had absolutely no experience in lake development and could pay less cash down, BTC chose IEI for several obvious reasons. Firstly, BTC had a good history with IEI. It was IEI's depository bank and primary lender since 1961, and IEI's president had a close relationship with BTC's president. Also, in the late 1960's IEI, with acquisition "loans" from BTC, bought two other struggling companies and thereby bailed out BTC on several bad loans. Secondly, BTC was aware of MIL's critical need for additional financing. BTC thought that IEI, despite its own financial problems, had a better chance of getting a development loan (which could be used in part to repay

BTC) or having enough money to keep MIL going until a buyer of substance could be found. BTC was aware of IEI's success in raising money from the sale of Thrift Certificates). Thirdly, Woodland principals (who now claim that BTC tricked them into believing that they had some continuing liability on an expired 1970 option contract) were willing to guaranty a portion of an acquisition loan to IEI.

IEI and BTC closed the sale on March 31, 1971. IEI got a terrible deal, but BTC fared much better. The $950,000 of delinquent Woodland Operations Loans were wiped off BTC's books—"paid" on paper by the $950,000 purchase price of the MIL Stock. $130,000 of the purchase price was paid in cash, and the $820,000 balance was "current" (safe from immediate charge-off) and owed by a company "better off than [Woodland]". However, BTC knew it was not "out of the woods"—it still had a large potential loss, and its collateral (the MIL Stock) "wasn't worth a damn" unless Lake Panorama was developed "at a terrific profit"—but BTC sold the MIL Stock to IEI (and financed the sale with a "risky" loan "it wouldn't have [otherwise] made") hoping that IEI could keep MIL going and make some loan payments and sell or refinance MIL and pay BTC with the proceeds.

F. Purchase Terms and Documents

The purchase price of the MIL Stock was paid as follows: (1) $130,000 cash at closing, at least $100,000 of which was Thrift Certificate proceeds; (2) IEI's "Collateral Pledge Note" (Acquisition Note") for $575,000; and (3) 50,000 shares of IEI common stock ("IEI Stock") valued at $245,000.

The Acquisition Note called for quarterly payments and a balloon on September 1, 1972. It was secured by the

MIL Stock, and BTC knew that possession of the MIL Stock, plus stock powers endorsed in blank by IEI, gave BTC the power to transfer the MIL Stock to itself or a purchaser (without foreclosure) if IEI defaulted. BTC also received an "Irrevocable Proxy" ("MIL Proxy") to vote the MIL Stock whenever IEI was in default on the Acquisition Note (virtually all the time). BTC demanded the MIL Proxy because of its concern over the outcome of the sale of the MIL Stock to IEI. In the words of BTC's president, "It was a nice comfortable instrument to have". (He found this to be so in January of 1971 with a predecessor proxy. *Supra* at 6.) BTC knew that the MIL Proxy gave it the unilateral power to call meetings, remove and elect directors and officers, amend articles and by-laws and generally control the affairs of MIL. (Because MIL was IEI's principal asset—it dwarfed IEI—the MIL Proxy was as compelling to IEI as it was to MIL.) According to BTC's senior loan officer, the MIL Proxy was "unique" and not something used before or since by BTC. It was against his practice to take a proxy, because "exercising" one would amount to conducting a borrower's business.

The $245,000 of IEI Stock received by BTC was 17-18% of IEI's widely-held voting stock. The next largest stockholder owned 4%. BTC knew that the IEI Stock entitled it to receive dividends on the IEI Stock and IEI stockholder communications and to attend and call stockholder meetings. It also knew that "many corporations *are controlled by less than a 50% ownership.*" (BTC received dividends on the IEI Stock and stockholder communications and, in effect, voted the IEI Stock by giving its proxy on three occasions to "educated"[1] IEI manage-

[1] According to BTC's president, IEI's management knew what BTC's "wishes were on almost anything in relation to [IEI and MIL]" and they "knew what BTC expected".

ment.) BTC could have increased the Acquisition Note by another $245,000 and not violated the admitted axiom that banks not own stock in their borrowers. Instead, BTC purposefully hid its ownership of the IEI Stock by registering it in the name of Bell & Co., a partnership of senior BTC officers. The IEI Stock was subject to a "put" option which gave BTC the right to require IEI to purchase the IEI Stock from BTC for $245,000. BTC admits that "puts" are unusual in the banking business.

An agreement ("Purchase Agreement") dated March 18, 1971, set forth other terms of the sale. It provided for yearly audited financials for IEI and MIL, quarterly unaudited financials (to better "track the operations of the companies"), additional information as and when desired by BTC and access by BTC to IEI's and MIL's books and records. It prohibited IEI from paying dividends[2] or selling substantial assets without BTC's consent. The Purchase Agreement also empowered BTC to require IEI to do a public offering of IEI capital stock to raise funds to pay the Acquisition Note and repurchase the IEI Stock. BTC's senior loan officer admits that this provision was very unusual and not used before or since by BTC. He is surprised that any borrower would give its bank such a power.

G. Keeping "Afloat"—Thrift Certificates and BTC

MIL was no less a mistake for IEI than the drug companies were for Woodland. Lake Panorama was underdeveloped and oversold, and the potential profits were

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[2] BTC approved a small dividend distribution in early 1972 (receiving $1,000 itself), even though IEI just reported a FY 1971 loss. BTC booked the dividend it received as non-loan income.

gone. IEI could neither afford to sustain the project nor let it die. No one would lend development monies, and buyers were not to be found. To make matters worse, IEI's president simultaneously committed IEI to two other expensive and full-time projects. One was a lake development project in southern Missouri called "Arrowhead Resorts, Inc." ("ARI"), and the other was a commercial office project in Des Moines called "West Bank". The long and involved story of how IEI survived for 3-½ years after purchasing the MIL Stock is summarized in the following paragraphs. The reasons it survived are Thrift Certificate proceeds and the actions and indulgences of BTC.

With its cash committed to sustaining its projects, IEI missed the first and second quarterly installments due BTC on the Acquisition Note. It had promised BTC to make a payment with the first advance of an $800,000 *ARI* development loan, but the prospective Missouri lender required a credit reference and "take-out" financing. BTC stepped in and vouched for IEI's creditworthiness and committed a $200,000 take-out loan. As a result, BTC received $65,000 of the *ARI* loan.[3] (BTC's president admits the purpose and result of this maneuver, but BTC's senior loan officer states that he never questioned the source of a loan payment, "not when you get paid".)

In February of 1972 BTC reviewed and wrote up IEI's and MIL's FYE 9-30-71 financial statements. The numbers were bad, but not unexpected—BTC had received interim financials and verbal reports. ("They kept us apprised of what was happening. We never had any

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[3] BTC never funded the take-out loan, and the ARI lender lost its money when ARI went bankrupt.

surprises from IEI.") IEI lost $26,300, and its current assets-to-current liabilities and debt-to-net worth ratios were 0.231:1 and 8.7:1, respectively. According to BTC, these are the two most important ratios, and they were "poor". BTC's write-up discussed Thrift Certificates by name, character ("one-year term, renewable at the option of the holder") and cumulative balance ($392,100) and noted the 300% increase from FYE 9-30-70. During the balance of 1972 BTC received quarterly financial statements and voluminous other financial documents, *e.g.*, lot sales reports, cash flow projections, expense reports, schedules of receivables, payables and investments and minutes of MIL board meetings. BTC relied on these documents and frequent verbal reports for day-to-day lending decisions. BTC was especially interested in documents regarding cash flow and cash source, because they showed BTC how it was going to be paid. One such document was IEI's break-even "Cash Flow Projection—April 1, 1972, to September 30, 1972". The "cash-out" section projected timely payment of the Acquisition Note and the "put" based on "cash-in" projections of $15,000 per month of net Thrift Certificate sales. (Thrift Certificates were obviously necessary to IEI's cash flow and to BTC's chances of being paid.) BTC also received at least one of IEI's 1972 (August) Thrift Certificate recap sheets showing monthly sales, redemptions and cumulative balances.

In April of 1972 IEI owed payments on notes it assumed when it purchased a venture-capital company named "Triple Eye" in 1971. BTC was the former depository bank and stock transfer agent for Triple Eye and was the escrow agent hired to receive and remit the Triple Eye note payments. IEI asked the Triple Eye noteholders to

trade their notes for Thrift Certificates.[4] Some wrote to BTC and declined the offer, but two noteholders (both Plaintiffs herein) mailed their notes to BTC, and BTC sent back Thrift Certificates. BTC's president admits that this transaction was passed by him before consummation.

In May of 1972 IEI "demoted" its president (decreased his duties) on account of his alcoholism and poor performance. His long-time relationship with BTC's president was a reason he was not fired. BTC was aware of his problems and the dissention he was causing. It was informed of his demotion in advance, and approved.

By summer of 1972 it was obvious that IEI could not pay the Acquisition Note or perform the "put" on September 1. BTC chose renewal over litigation and liquidation. It knew its only chance of substantial recovery was for IEI and its subsidiaries to stay in business. BTC hosted a luncheon for the ex-Woodland people who had guarantied a portion of the Acquisition Note (*supra* at 7) and then sent them a confirming letter stating that the Acquisition Note would not be renewed without their signed consent and that additional collateral would be given to secure the Acquisition Note (the obligation they guarantied) as well as the "put". Testimony and documents show that BTC intended to renew with or without the guarantors' consent and that renewal papers were already drafted (and would be signed) to only benefit the "put" with the new collateral, *i.e.*, BTC lied to the guarantors to get their signatures.

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[4] BTC received copies of the solicitation letters which enclosed newspaper advertisements for Thrift Certificates and pandered high interest rates and IEI's "unconditional guarantee".

The Acquisition Note and the "put" were renewed on September 30, 1972, for two years. The amended Purchase Agreement ("Amended Purchase Agreement") required an immediate $30,000 cash payment and a new installment balloon note ("Renewal Note") for the balance of the Acquisition Note. The "put" price was increased to $300,000, and an 11% "service charge" was added.[5] Also, the "put" was secured with ARI's voting stock (with blank stock powers signed by IEI) and junior mortgages on IEI's home office building and the West Bank project. The Amended Purchase Agreement required *monthly* consolidat*ing* (versus quarterly consolidated) financial statements for IEI and MIL and *each of their subsidiaries* (including IMF). It also prohibited large IEI borrowings without BTC's consent, so BTC could veto future unwise investments and partake of the proceeds of third-party loans. The $30,000 cash payment was made in Thrift Certificate proceeds. In fact, on September 30 (a Saturday) BTC's senior loan officer was given a $30,000 IMF check payable to IEI, an IEI deposit slip to its BTC checking account and a $30,000 IEI check to BTC, and he banked them the following Monday. In conclusion, the renewal of the Acquisition Note and the "put" gave BTC $30,000 cash, some collateral for the "put" (placing BTC further ahead of other creditors), another opportunity to bring the former Woodland Operations Loans "current" on its books and some additional information and controls over IEI.

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[5] BTC's senior loan officer initially structured the Amended Purchase Agreement to replace the IEI Stock with a $300,000 secured loan, but BTC's president quashed the change. (BTC would have lost its stockholder powers, and IEI did not need $300,000 more debt on its balance sheet.)

BTC reviewed and wrote-up IEI's FYE 9-30-72 financial statements in March of 1973. IEI lost $323,100 (twelve times more than FYE 9-30-71), and its debt-to-net worth ratio jumped to a worse-than-"poor" 13.26:1. BTC's write-up noted that IEI was "under extreme debt pressure and company leverage for creditors [was] severely limited". BTC's senior loan officer said this meant that IEI's debt was not serviceable from earnings and additional financing or capital was needed to service debt. As for additional financing, BTC's write-up also noted that "Thrift Certificates, one-year renewable at option of the holder amount to $694,970 up from $392,100 in 1971". IEI's statement disclosed another "rather significant event . . . lending wise" in BTC's opinion, *i.e.*, IEI's auditors prepared its 1972 financials on a "going concern basis". BTC knew this to mean that the balance sheet numbers were only accurate if IEI could stay in business, save its assets from secured creditors, find needed financing, resolve threatening lawsuits and become profitable; otherwise, IEI had no net worth. (BTC had long ago realized that, notwithstanding its collateral, it would lose big if IEI/MIL folded.) MIL's and ARI's FYE 9-30-72 statements were equally bad. During 1973 BTC received the same voluminous interim documents and frequent verbal reports as before plus the newly required *monthly* consolidating financial statements ("trial balances"). The "trial balances" exposed large and increasing Thrift Certificates sales, IMF's portfolio of unsecured IEI notes and IMF's negative net worth since 9-30-72.

In April of 1973 IEI had to either unload the West Bank project or go down with it. It needed the help of BTC and its earlier-demoted president (the son-in-law of

a major West Bank creditor). BTC agreed to trade its then worthless West Bank mortgage (recently received to secure the "put") for a good $12,000 note receivable, and it consented to the "sale" of an IEI owned real estate service company to IEI's president (to buy him off). ($91,500 of Thrift Certificates were sold/renewed in April of 1973.)

By May of 1973 IEI was in default on the first and second quarterly payments on the Renewal Note, on the service charge on the "put" and on two older BTC loans. Fearing this $71,000 delinquency would close IEI's doors, BTC's president orchestrated an unusual transaction "to keep IEI in business". He required IEI to borrow $71,000 from BTC and use the loan proceeds to "pay" $71,000 to BTC. He also required MIL to issue a $71,000 note to IEI so IEI could pledge it on its "new" $71,000 loan from BTC. Finally, he required IEI to secure a previously unsecured operating loan with the MIL Stock. The $71,000 loan was a fiction and a "wash". In effect, BTC loaned $71,000 to itself to keep IEI going. It also turned delinquent loans into "current" loans and got more collateral to put itself further ahead of general creditors *e.g.*, Thrift Certificate holders. In BTC's words, it was "weathering the storm"; its collateral "wasn't worth a damn" if IEI and MIL closed their doors. ($52,000 of Thrift Certificates were sold/renewed in May of 1973.)

In August of 1973, shortly after missing the third quarterly Renewal Note and service charge payments, IEI had to sell its home office building. BTC approved the sale in return for the net sales proceeds. $50,000 was paid on the "put", and $23,965.46 was paid on the Renewal Note (which was not even secured by the building). IEI hid the

sale from Thrift Certificate holders/purchasers so as not to alarm them. ($367,000 of Thrift Certificates were sold/renewed in June, July and August of 1973.)

By November of 1973 the "energy crisis" had all but stopped MIL's and ARI's sales of lake lots. In the words of BTC's president, the recreational lot business "collapsed", and MIL "fell flat on its face". IEI also missed the fourth quarterly Renewal Note and service charge payments. On November 19 IEI's new president met with BTC's president and senior loan officer to review IEI's situation. Recent financials showed large delinquent obligations and a large cash deficit. A current Thrift Certificate recap sheet and "trial balance" exposed accelerated Thrift Certificate sales and a larger negative net worth for IMF. IEI's president was told to report back the next day with figures showing the "cash required by IEI and its subsidiaries to put all of the companies on a sound financial basis". On November 20 he reported that MIL and ARI each needed $2,500,000 and IEI needed $1,122,465. BTC was not surprised. It had always known about the critical need for (and absence of) large development loans. It had counted on receiving a large portion of any development loan. It had reviewed IEI's third-party loan applications, offered suggestions and even contacted potential lenders. ($313,500 of Thrift Certificates were sold/renewed in September, October and November of 1973.)

In late November, 1973, an Omaha lender refused MIL's urgent request to release monies from a reserve account securing factored real estate contracts. In early December BTC's president accompanied IEI's president to Omaha in search of a "solution to [MIL's] problems". They came back with monies from the reserve account, and MIL paid some pressing bills.

On December 31, 1973, BTC made a secured, $69,000 "emergency" loan to IEI to pay delinquent, existence-threatening real estate taxes. In BTC's words, "At this time everything [IEI] was doing was emergency". ($66,500 of Thrift Certificates were sold/renewed in December of 1973.)

In March of 1974 BTC's president helped IEI collect a note receivable by making written demand on the maker. He falsely stated that BTC owned the note. The resulting $13,000 payment was applied to the "put", even though BTC had not exercised "put".

BTC did everything it could in early 1974 to keep IEI and MIL going for another sales season without "exposing [itself] any greater", because it knew what would happen to its loans and collateral if they failed. "To keep [IEI and MIL] going" and to improve its position *vis-a-vis* other creditors, BTC orchestrated another unusual "loan" transaction. It required MIL to issue a $25,000 note to IEI and IEI to pledge the note to secure the unpaid balance of IEI's May 1973 $71,000 "loan" (*supra* at 15). It also required MIL to borrow $46,000 from BTC to pay IEI so IEI could use the money, plus $16,000 of other funds, to pay BTC and bring its loans "current". (The other funds turned out to be Thrift Certificate proceeds.) BTC also required IEI to pledge its stock in a plastics company to secure another old loan. "[BTC's] primary purpose was to try to keep both organizations afloat", so it could receive more money. It also got $16,000 cash and more collateral; $46,000 of IEI debt was transferred to MIL (who had a better financial statement); and the Woodland Operations Loans (now IEI and MIL obligations) were "current" once again. On March 25 BTC's president and senior loan officer attended IEI and MIL board meetings. After

reviewing financial statements[6] with directors and auditors, BTC's president demanded and received additional collateral—"as much as [BTC] could get"—including ARI notes and voting stock of another subsidiary. He also required MIL to borrow another $25,000 from BTC and pay it to IEI so IEI could pay the balance of the May 1973 $71,000 "loan". ($439,600 of Thrift Certificates were sold/renewed in January, February and March of 1974.)

In April of 1974 IEI defaulted on the sixth consecutive Renewal Note payment, and BTC reviewed and wrote-up IEI's FYE 9-30-73 "going-concern" financial statements. IEI had a record $400,000 loss, and the Thrift Certificate balance had doubled to $1,142,909. ($141,200 of Thrift Certificates were sold/renewed in April of 1974.)

On or about May 10, 1974, IEI's president met with BTC's president and senior loan officer to inform them of a change in the Iowa securities laws which prohibited the future sale and renewal of Thrift Certificates without registration.

In July of 1974 IEI was preparing to file bankruptcy for itself and its subsidiaries. On July 23 BTC's president, armed with the IEI Stock, the MIL Stock and the MIL Proxy, attended a joint IEI-MIL board meeting and vetoed a proposal to put MIL in bankruptcy. He thought it would destroy the value of the MIL Stock, BTC's collateral. IEI, IMF and ARI filed bankruptcy on August 22, 1974, but not MIL. On August 20 BTC used a dummy

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[6] The financials showed large losses, a big decline in IEI's "going-concern" (imaginary) net worth and a huge increase in Thrift Certificate sales—the Thrift Certificate balance went from $694,970 at FYE 9-30-72 to $1,142,909 at 9-30-73 to $1,443,745.87 on March 25, 1974.

corporation called "Aquarius, Inc." to "buy" the Renewal Note and collateral therefor (MIL Stock) and the "put" with a 100% acquisition "loan" from BTC. Aquarius was owned and staffed (on paper) by non-bank businessmen but was run by BTC's president as BTC's "alter ego". The debt of Woodland (and then of IEI) was "current" once again, and BTC was firmly in control of its new "borrower". (BTC admitted in depositions that it never used anything like Aquarius before.) BTC's president, wearing his Aquarius hat and waving the MIL Proxy, then set about to "effect [MIL] management by friendly persuasion". First he made it clear to MIL management that he could "rock the boat" (meaning "fire everybody, hire new people") if not satisfied with their performance. Then he told MIL's management that liquidation was not desirable and that "[MIL] should stay operational as [MIL] was the primary salvation in order for Aquarius, Ltd. [/BTC] to recover on [IEI's] debt". Then he returned to Omaha with MIL's president to see if the Omaha bank would put up some more money to salvage MIL, and, when the Omaha bank balked because of its distrust for MIL management, BTC conducted the firing of MIL's president and the addition of a new member to the MIL board. A few months later BTC gave up, and MIL sunk into bankruptcy.

H. BTC's Benefit and Knowledge

BTC did not really "lose over $650,000 . . . due to IEI's insolvency"[7] in 1974, as it insists in its petition; it

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[7] The District Court apparently understood that a $650,000 loss was "undisputed" by Plaintiffs. (Appendix to BTC's petition at A-14.) This is incorrect.

really lost $950,000 in 1970 due to Woodland's insolvency and eventually got it all back *from IEI*. BTC received a $130,000 cash down payment on the MIL Stock. It received payments totalling $368,000 on the Acquisition/Renewal Note and the "put"; $320,000 of this amount was cash *not* borrowed from BTC. BTC received dividends of $1,000 on the IEI Stock. After IEI's bankruptcy BTC collected $12,000 on the "put" (liquidation of collateral), another $117,000 from the bankruptcy trustee and another $400,000 from the guarantors of the Acquisition/Renewal Note. By accruing interest and service charges on a moneyless "loan", BTC creates a paper loss that hides a remarkable recovery—approximately $980,000 cash on $950,000 of Woodland Operations Loans.

BTC's successes, large or small, are at least partially a result of Thrift Certificates. Many thousands of dollars of Thrift Certificate proceeds were paid by IEI to BTC, and IEI could not have lived so long and given so much money and collateral to BTC without the Thrift Certificate program.

Despite its vehement denial, BTC was extremely knowledgeable about Thrift Certificates. It knew what they were, how they were sold and whom they benefited. BTC knew about IMF, its assets and its negative net worth. It knew about IEI's worthless "unlimited guarantee" of the Thrift Certificates. It knew that IEI, a company that could not pay its obligations as they matured and whose liabilities exceeded the liquidation value of its assets, was selling unsecured Thrift Certificates at a vigorous rate. It knew that Thrift Certificates were unregistered and unmonitored because of a serious "deficiency" in the Iowa securities laws. The "moral" aspects of Thrift Certificate-

type securities bothered BTC. "[T]he small fellow with a few bucks—a few dollars that wanted to make more than he could at the bank was—you know, he was led into the thing and figured that he made a big deal." BTC thought that Iowans were gullible. "It has always amazed me how in the great state of Iowa people were able to hock stock . . . without any real information being passed off to prospective purchasers, so [large Thrift Certificate sales] did not surprise me."

I. Summary of BTC's Power to Control

BTC's power to control IEI is primarily a function of its ownership/possession of the IEI Stock, the MIL Stock and the MIL Proxy and the purposes, uses and implications thereof. BTC's unusual relationship to IEI is also indicative of control. In the opinion of BTC's senior loan officer, a debtor's primary lender "can exert any kind of pressure" it wants. BTC was IEI's "largest lender" and "principal lender", and IEI knew that BTC could have "pulled the plug any time". BTC's president had a good relationship with IEI management. He "had access to the officers"; if he "needed anything from [IEI] . . . [he] could have accomplished it". IEI's management knew what BTC's "wishes were on anything in relation to [IEI and MIL]" and "knew what BTC expected". BTC management was in almost daily contact with BTC, and BTC "never had any surprises".

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REASONS FOR DENYING THE WRIT

THIS COURT SHOULD NOT GRANT CERTIORARI WHEN THE DECISION OF THE COURT OF APPEALS IS NOT IN CONFLICT WITH DECISIONS OF OTHER COURTS OF APPEALS OR WITH PRIOR DECISIONS OF THIS COURT, IS INTERLOCUTORY AND AFFECTS ONLY THE PARTIES TO THIS ACTION, AND IS BASED UPON A FACT QUESTION IN THE CONTEXT OF APPROPRIATE SUMMARY JUDGMENT STANDARDS CORRECTLY APPLIED.

In seeking to persuade the Court to exercise its extraordinary and discretionary certiorari jurisdiction, BTC seizes upon isolated statements in the opinion of the Court of Appeals and contends that court's decision "effectually" contravenes this Court's prior decision in *Ernst & Ernst v. Hochfelder,* 425 U.S. 185 (1976), and conflicts with the decisions of the Third and Fifth Circuits in *Monsen v. Consolidated Dressed Beef Co.,* 579 F.2d 793 (3d Cir.), *cert. denied,* 439 U.S. 930 (1978), and *Woodward v. Metro Bank of Dallas,* 522 F.2d 84 (5th Cir. 1975). These contentions are neither meritorious nor sufficiently significant to warrant the grant of certiorari.

The biggest hurdle confronting BTC is the absence of any real dispute concerning the applicable legal standards. The standards utilized by the Eighth Circuit in this case are consistent with the scienter requirement delineated in *Hochfelder* and the aiding and abetting principles expressed in *Monsen* and *Woodward.* Indeed, the Court of Appeals expressly agreed with BTC concerning the proper legal standards to be applied. However, based upon its careful review of the voluminous record, it concluded that a jury issue did exist concerning aiding and

abetting liability, and for that reason set aside the grant of summary judgment in BTC's favor on that issue. In actuality, BTC's disagreement with the facts and the inferences to be drawn therefrom is the only real issue raised in its petition.

In examining the legal standards governing liability for aiding and abetting violations of the securities laws, the Court of Appeals reiterated the three-pronged test previously adopted by that circuit in *Stokes v. Lokken,* 644 F.2d 779 (8th Cir. 1981), and generally recognized by the federal courts. By its own terms, this standard is completely consistent with the scienter requirement of *Hochfelder.* As the court in *Stokes* observed in adopting this test, *Hochfelder* "clearly eliminates negligence as a possible basis for a finding of liability . . . ." *Stokes,* 644 F.2d at 783. The Eighth Circuit's thorough discussion of the standard in this case leaves no doubt that aiding and abetting liability cannot be predicated upon negligence. *Metge v. Baehler,* Appendix to Petition for Certiorari at A-3-6, 762 F.2d 621, 624-25 and n. 1 (8th Cir. 1985). Indeed, the court specifically held that a "high standard of intent" and "high scienter standard" must be satisfied at trial before liability may be imposed on BTC. *Id.* This standard of liability comports with the scienter requirement of *Hochfelder.*

It is also apparent that the liability standard utilized by the Eighth Circuit is consistent with that employed by the Third and Fifth Circuits in *Monsen* and *Woodward, supra.* In fact, the Court of Appeals expressly adopted the formulations of aiding and abetting liability set forth in those decisions. *Metge,* Appendix to Petition for Certiorari at A-4-6, 762 F.2d at 624-25. Nothwithstanding

BTC's protestations to the contrary, the legal standards applied by the Court of Appeals do not deviate in any way from *Hochfelder, Monsen* or *Woodward.* Therefore, the petition does not present a sufficiently significant question to warrant the exercise of this Court's extraordinary and discretionary certiorari jurisdiction.

The only real question raised in BTC's petition concerns the application of undisputed legal standards to the particular facts of this case and is of interest only to the parties actually involved. BTC's petition constitutes nothing more than a dispute between it and the Court of Appeals as to what the facts are or may be found to be and an attempt to draw the Court into a reevaluation of those facts and the inferences to be drawn therefrom. Fact canvassing of this nature is not the purpose of a grant of certiorari.

> Certiorari is granted only "in cases involving principles the settlement of which is of importance to the public as distinguished from that of the parties, and in cases where there is a real and embarrassing conflict of opinion and authority between the circuit courts of appeal."

N.L.R.B. v. Pittsburgh Steamship Co., 340 U.S. 498, 502 (1951) (*quoting Layne & Bowler Corp. v. Western Well Works,* 261 U.S. 387, 393 (1923)). "Granting of the writ would not be warranted merely to review the evidence or inferences drawn from it." *General Talking Pictures Corp. v. Western Electric Co.,* 304 U.S. 175, 178 (1938).

The inappropriateness of a grant of certiorari in these circumstances is heightened because the evidentiary review requested by BTC would perforce require this Court to enter into a factual quagmire. This case is based upon complicated and voluminous facts. The record

includes over 13,900 documents and over 9,000 pages of deposition testimony. The appendix filed in the Court of Appeals was 2405 pages. The time consuming evidentiary review which would be required of the Court cannot be justified where no conflicting legal principles are involved. Further review by the Court is unwarranted.

Additional factors also militate against the grant of certiorari in this case. The Eighth Circuit's decision only reversed the district court's grant of summary judgment in BTC's favor on the aiding and abetting claim. No actual findings of fact have been made in this case, and there has been no imposition of liability. Rather, the Court of Appeals, after a careful review of the record as a whole, has merely concluded that a jury question is presented. Where the sole result of the Eighth Circuit's decision is a remand for trial on the merits pursuant to generally accepted standards of liability, the decision is properly significant only to the parties involved. In these circumstances, plenary consideration by this Court is premature and unnecessary.

The Court of Appeals also applied the appropriate standard in reviewing and reversing the grant of summary judgment. As evidenced by its detailed opinion, the court carefully evaluated the complex and voluminous record and found there to be sufficient evidence to present a jury question concerning BTC's liability for aiding and abetting the primary securities violations. The record firmly supports this conclusion. It shows, and a jury can properly find, the following: BTC embarked on an unusual and continuing course of conduct to recover large and unusual loan losses from a borrower; by this course of conduct BTC substantially assisted the borrower's primary violations of the anti-fraud provisions of the

federal securities laws; BTC was aware of the primary violations and its assistance thereto and role therein; BTC consciously intended to assist in the primary violations or had a conscious and specific motivation for not acting to stop or disclose the primary violations; and BTC knowingly benefited from the primary violations.

The main thrust of the petition is a claim that there is no evidence that BTC knew the primary violations were being committed. As is true in many securities fraud cases, particularly those involving secondary liability, Plaintiffs must prove critical state-of-mind facts, such as knowledge, intent and motive, by inferences and circumstantial evidence. *E.g., Woodward,* 522 F.2d at 96. The evidence outlined in the Statement of Facts section of this brief and by the Court of Appeals provides a basis from which a jury could properly infer and conclude that BTC knew of the primary violations and knowingly and substantially assisted therein.

Finally, the decision of the Court of Appeals will in no way chill or proscribe normal and legitimate banking activities. In this case BTC went far beyond routine and acceptable loan collection practices. It involved itself intimately in the affairs of its borrower, assisted in a fraud on the borrower's other, less sophisticated creditors through a series of unusual, manipulative and disguised transactions and knowingly benefited therefrom. BTC's actions place it beyond the boundaries of normal and legitimate banking activities. The Court of Appeals recognized this in its tightly-worded opinion. Lending institutions engaged in ordinary and legitimate banking activities need not be alarmed.

CONCLUSION

The petition presents no substantial issues for review by this Court. The legal standards utilized by the Court of Appeals in reversing the grant of summary judgment are consistent with the prior decisions of this Court and are generally accepted by the lower federal courts. In actuality, the only real issues raised by the petition center on the particular facts of this case and are of concern only to the parties involved. The inappropriateness of a grant of certiorari in such circumstances is well-recognized. A grant of the writ in this case would be particularly inappropriate given the voluminous and complex factual record involved. The fact that this matter arises in the context of summary judgment and that trial on the merits is yet to occur further marshalls against review by this Court at this time. In these circumstances, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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